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IN THE

SUPREME COURT OF THE UNITED STATES

October Term, 1987

D. H. HOLMES CO., LTD.,

Appellant,

v.

SHIRLEY McNAMARA,
SECRETARY OF REVENUE & TAXATION,
THE DEPARTMENT OF REVENUE & TAXATION,
STATE OF LOUISIANA,

Appellee.

**On Appeal from the Court of Appeal,
Fourth Circuit, State of Louisiana**

BRIEF OF THE AMERICAN RETAIL FEDERATION AS *AMICUS CURIAE* IN SUPPORT OF APPELLANT

MARYANN B. GALL
(Counsel of Record)
NANCY TRUITT BLOSSER
LAURA A. KULWICKI
JONES, DAY, REAVIS & POGUE
1900 Huntington Center
41 South High Street
Columbus, Ohio 43215
(614) 469-3939

Counsel for Amicus Curiae

COURT INDEX PRESS, INC. — 215 E. Ninth Street, Cincinnati, Ohio 45202 — (513) 241-1450

TABLE OF CONTENTS

	Page
INTEREST OF AMICUS CURIAE	1
STATEMENT OF THE CASE	3
SUMMARY OF ARGUMENT	7
ARGUMENT	8
I. LOUISIANA'S ATTEMPT TO TAX APPELLANT'S OUT-OF-STATE ACTIVITIES VIOLATES THE DUE PROCESS CLAUSE OF THE UNITED STATES CONSTITUTION.	8
II. THE APPLICATION OF LOUISIANA'S USE TAX TO THE DISTRIBUTION OF INFORMATIONAL CATALOGS THROUGH THE MAIL CONSTITUTES AN IMPERMISSIBLE BURDEN ON INTERSTATE COMMERCE IN VIOLATION OF THE COMMERCE CLAUSE.	19
CONCLUSION	27

TABLE OF AUTHORITIES

Cases: Page

ASARCO, Inc. v. *Idaho State Tax Comm'n*, 458 U.S. 307 (1982) 11

American Oil Co. v. *Neill*, 380 U.S. 451 (1965) 8, 16

Cleveland, Painesville & Ashtabula R.R. Co. v. *Commonwealth of Pennsylvania*, 82 U.S. 179, (15 Wall. 1873) 10

Commonwealth Edison Co. v. *Montana*, 453 U.S. 609, *reh'g denied*, 453 U.S. 927 (1981) 21

Complete Auto Transit, Inc. v. *Brady*, 430 U.S. 274, *reh'g denied* 430 U.S. 976 (1977) 7, 8, 19, 20, 21, 23, 25, 27

Connecticut Gen. Life Ins. Co. v. *Johnson*, 303 U.S. 77 (1938) 10, 11

County of Mobile v. *Kimball*, 102 U.S. 691 (1881) 19

D.H. Holmes Co. v. *McNamara*, ___ U.S. ___, 108 S. Ct. 283 (1987) 4

Dep't of Revenue v. *Ass'n of Washington Stevedoring Cos.*, 435 U.S. 734 (1978) 20, 21

Exxon Corp., v. *Dep't of Revenue*, 447 U.S. 207 (1980) 21

Farmers Loan & Trust Co. v. *Minnesota*, 280 U.S. 204 (1930) 10

General Motors Corp. v. *Washington*, 377 U.S. 436, *reh'g denied*, 379 U.S. 875 (1964) ... 8, 16, 17

Great Atlantic & Pacific Tea Co. v. *Grosjean*, 301 U.S. 412 (1936), *reh'g denied*, 302 U.S. 772 (1937) 11

Page

Henneford v. *Silas Mason Co.*, 300 U.S. 577 (1937) 9, 11, 12

Indiana Dep't of State Revenue v. *Frank Purcell Walnut Lumber Co.*, 152 Ind. App. 122, 282 N.E.2d 336 (1972) 19

James v. *Dravo Contracting Co.*, 302 U.S. 134 (1937) 11

Japan Line, Ltd. v. *County of Los Angeles*, 441 U.S. 434 (1979) 20

McGoldrick v. *Berwind-White Coal Mining Co.* 309 U.S. 33 (1940) 23

McLeod v. *J.E. Dilworth Co.*, 322 U.S. 327 (1944) 9

McNamara v. *D.H. Holmes Co.*, 505 So.2d 102 (La. App. 1987), *cert. denied*, 506 So.2d 1224 (1987) 4

McNamara v. *D.H. Holmes Co.*, 505 So.2d 102 (La. App. 1987) 4, 12, 13, 14, 15, 23

Miller Bros. Co. v. *Maryland*, 347 U.S. 340 (1953), *reh'g denied*, 347 U.S. 964 (1954) 8, 23

Minnesota v. *Clover Leaf Creamery Co.*, 449 U.S. 456, *reh'g denied*, 450 U.S. 1027 (1981) (citation omitted) 25

Moorman Manufacturing Co. v. *Bair*, 437 U.S. 267, *reh'g denied*, 439 U.S. 885 (1978) 21

National Bellas Hess v. *Dep't of Revenue*, 386 U.S. 753 (1967) 19, 25

National Geographic Society v. *Calif. Bd. of Equalization*, 430 U.S. 551 (1977) 9

Page

Norton Co. v. *Dep't of Revenue*,
340 U.S. 534 (1951) 7, 15, 16, 17, 18

Pennsylvania v. *West Virginia*,
262 U.S. 553 (1923) 19

Pike v. *Bruce Church, Inc.*,
397 U.S. 137 (1970) 25

Robbins v. *Shelby County Taxing Dist.*,
120 U.S. 489 (1887) 19

Scripto, Inc. v. *Carson*,
362 U.S. 207 (1960) 8

Standard Pressed Steel Co. v. *Dep't of Revenue*,
419 U.S. 560 (1975) 17

Steamship Co. v. *Portwardens*,
73 U.S. 31 (6 Wall. 1867) 19

Sullivan v. *United States*,
395 U.S. 169 (1969) 9

Tyler Pipe Industries, Inc. v. *Washington*,
___ U.S. ___, 107 S. Ct. 2810 (1987) 16

Welton v. *Missouri*,
91 U.S. 275 (1876) 19

Western Live Stock v. *Bureau of Revenue*,
303 U.S. 250 (1938) 25

Western Union Tel. Co. v. *Pendleton*,
122 U.S. 347 (1887) 19

Constitution of the United States:

Article I, Section 8, Clause 3 ..... 3, 19

Amendment XIV, Section 1 ..... 3, 8, 10

Page

United States Code Annotated:

18 U.S.C.A. § 1708 13

Louisiana Revised Statutes Annotated:

La. Rev. Stat. Ann. § 47:301(18) 11

La. Rev. Stat. Ann. § 47:302(A)(2) 4-5, 9

La. Rev. Stat. Ann. § 47:305(E) 6

La. Rev. Stat. Ann. § 47:321(A) 5

La. Rev. Stat. Ann. § 47:321(C) 5

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INTEREST OF *AMICUS CURIAE*

American Retail Federation was founded in 1935 to provide retailers with a unified and central voice for rapid and effective response to government regulations and policies affecting the industry and its customers. Headquartered in Washington, D.C., the Federation serves as an umbrella organization encompassing a variety of large and small retailers, state retail associations, and national retail associations. The Federation's uniqueness is in the nature of this membership, which includes fifty state retail associations, twenty-four national retail associations, and corporate retailers ranging from the largest general merchandise department stores and discount store chains to small specialty stores. The retail industry accounts for nearly one-quarter of the

gross national product and employs over sixteen million persons.

The Federation is critically concerned with the Court of Appeal of Louisiana's decision in this case, which the Federation submits is in error. The State of Louisiana's view of the reach of its taxing jurisdiction distorts this Court's Due Process and Commerce Clause jurisprudence in the context of taxation and causes a severe disruption in both the flow of mail in interstate commerce and the ability of retailers and others (both profit and non-profit entities) to use direct mailings to communicate promotional or other information to the citizens of this country. Because this Court's decision will have a direct effect on matters of prime importance to the Federation and its members, the Federation submits this brief to assist the Court in its resolution of the case.[1]

[1] Pursuant to Sup. Ct. R. 36, the parties have consented to the filing of this brief. Their letters of consent have been filed with the Clerk of the Court.

STATEMENT OF THE CASE

This case concerns the power of a state to levy a use tax against a taxpayer's activities which are not fairly related to the taxing state. In this case, the State of Louisiana is in effect levying tax on D.H. Holmes Company, Ltd. ("Holmes") for the distribution by the U.S. Postal Service to state residents of direct mail informational catalogs printed out-of-state. In levying this use tax against Holmes, the State of Louisiana has exceeded its jurisdictional taxing power, as limited by both the Due Process Clause, U.S. Const. amend. XIV, § 1, and the Commerce Clause, U.S. Const. art. I, § 8, cl. 3. The state has improperly linked an in-state use of property to the wrong taxpayer.

Holmes is a retailer with stores in Louisiana, Alabama, and Mississippi. (Joint App. 54-55, 68-69, 78-79, 80-81). To advertise the goods it has for sale in its stores, Holmes purchases catalogs to send to its charge account customers. (Joint App. 54-55, 71-73, 75-76, 89, 38-39). The creative work of designing Holmes' catalogs is done in New York City by advertising agencies. (Joint App. 70-71, 83-85). On Holmes' behalf, the agencies purchase paper for the catalogs, contract for their printing, and arrange for mailing to Holmes' customers. All catalogs are printed in either Atlanta, Boston, or Oklahoma City and mailed from those points. (Joint App. 57-58, 74, 80, 81, 83-87, 88, 90, 91). The printers deliver the completed catalogs to the post office and Holmes pays the postage by sending checks to the post offices in these cities. (Joint App. 81-82).

During the period 1979 through 1981, Holmes purchased nineteen merchandise catalogs for a total amount of $2,024,000. The Secretary of Revenue and Taxation of Louisiana audited Holmes and assessed it "delinquent Louisiana general sales tax," *inter alia*, on the invoices rendered to Holmes for its catalog purchases.[2] The Secretary of Revenue

[2] The assessment was levied on the eighty-two percent of merchandise catalogs that were mailed to Holmes' customers in Louisiana. Eighteen per-

and Taxation then instituted an action in the Civil District Court of Orleans Parish to collect the tax. (Joint App. 54-55, 78-79, 80-81). (Petition for Payment of Delinquent Taxes and Ex. A thereto, Joint App. 2-7). Holmes contended from the outset that the tax "violates the interstate commerce clause of the constitution of the United States of America . . . ." (Defendant's Answer to Petition for Payment of Delinquent Taxes, Joint App. 11-13). The trial court sustained the assessment.

The Louisiana Court of Appeal, Fourth Circuit, affirmed. *McNamara* v. *D.H. Holmes Co.*, 505 So.2d 102 (La. App. 1987). The Louisiana Supreme Court refused further review. *McNamara* v. *D.H. Holmes Co.*, 505 So.2d 102 (La. App. 1987), *cert. denied*, 506 So.2d 1224 (1987). Jurisdiction was noted by this Court in *D.H. Holmes Co.* v. *McNamara*, ____ U.S. ____, 108 S. Ct. 283 (1987).

The tax in question was levied in these terms:

> A. There is hereby levied a tax upon the sale at retail, the use, the consumption, the distribution, and the storage for use or consumption in this state, of each item or article of tangible personal property, as defined herein . . .
>
> (1) At the rate of two per centum (2%) of the sales price of each item or article of tangible personal property when sold at retail in this state; . . .
>
> (2) At the rate of two per centum (2%) of the cost price of each item or article of tangible personal property when the same is not sold but is used, consumed, distributed or stored for use or consumption in this state; provided there shall be no duplication of the tax.

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cent of the catalogs were sent to Alabama and Mississippi customers and were not taxed. (Joint App. 54-55, 78-79, 80-81).

La. Rev. Stat. Ann. § 47:302(A)(2) (West 1987). An additional one percent tax is imposed by La. Rev. Stat. Ann. § 47:321(A).[3]

The tax "shall be collected from the dealer, as defined herein, [and] shall be paid at the time and in the manner hereinafter provided . . . ." La. Rev. Stat. Ann. § 47:302 (C).[4]

The "dealer" is directed to collect the tax from "the purchaser or consumer."[5] For sales taking place *outside* Louisiana:

> Every dealer located outside the state making sales of tangible personal property for distribution, storage, use, or other consumption, in this state, shall at the time of making sales collect the tax imposed by this Chapter from the purchaser.

La. Rev. Stat. Ann. § 47:304(B).

Dealers are ordered "as far as practicable, [to] add the amount of the tax imposed under this chapter . . . to the sale price or charge, which shall be a debt from the purchaser or consumer to the dealer, until paid, and shall be recoverable at law in the same manner as other debts." La. Rev. Stat. Ann. § 47:304(C).

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[3] The additional one percent tax levied by La. Rev. Stat. Ann. § 47:321 (A) also "shall be collected from the dealer, and/or wholesaler as provided for and defined by said Chapter 2 of Title 47; shall be paid at the time and in the manner provided by said Chapter; . . ." La. Rev. Stat. Ann. § 47:321 (C).

[4] The additional one percent tax levied by La. Rev. Stat. Ann. § 47:321(A) also "shall be collected from the dealer, and/or wholesaler as provided for and defined by said Chapter 2 of Title 47; shall be paid at the time and in the manner provided by said Chapter; . . ." La. Rev. Stat. Ann. § 47:321(C).

[5] La. Rev. Stat. Ann. § 47:301(4) defines a "dealer" as "every person who manufactures or produces tangible personal property for sale at retail, for use, or consumption, or distribution or for storage to be used or consumed in this state."

Louisiana specifically recognizes the constitutional limitations upon its power to impose tax:

> nor is it the intention of this Chapter to levy a tax on bona fide interstate commerce. It is, however, the intention of this Chapter to levy a tax on the sale at retail, the use, the consumption, the distribution, and the storage to be used or consumed in this state, of tangible personal property after it has come to rest in this state and has become a part of the mass of property in this state.

La. Rev. Stat. Ann. § 47:305(E).

SUMMARY OF ARGUMENT

Louisiana's use tax levy upon Holmes' out-of-state activities violates the Due Process Clause of the Constitution because Louisiana lacks transactional nexus with the activities it seeks to tax. Louisiana lacks the requisite nexus in several respects. First, Louisiana impermissibly attempts to tax transactions and activities occurring wholly beyond its jurisdiction. Second, the taxed activity, the use of the promotional materials within the state, is not sufficiently connected to Holmes, the party against whom the tax is assessed. Finally, Holmes' local retail operations do not create nexus sufficient to tax activities unrelated to this local business. Holmes' activities in arranging the production, printing, and mailing of catalogs to Louisiana residents from out of state is a transaction that is clearly interstate in character. Because these activities are dissociated from Holmes' local business and are interstate in nature, they lack the nexus required to support taxation by Louisiana. *Norton Co.* v. *Dep't of Revenue*, 340 U.S. 534 (1951).

The application of Louisiana's use tax to Holmes' distribution of promotional materials through the mail also constitutes an impermissible burden on interstate commerce in violation of the Commerce Clause. In upholding the tax, the Louisiana court improperly applied the test in *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. 274 (1977). Louisiana lacks a sufficient nexus with Holmes' out-of-state activity, and therefore the first requirement of *Complete Auto's* four-part test is not met. Moreover, Louisiana's tax on the actual movement of mail through the interstate mail system unfairly burdens interstate commerce and the remote mail sender who uses that system. Since the Louisiana use tax, as applied in this case, violates both the Due Process and the Commerce Clause of the United States Constitution, the judgment below should be reversed.

ARGUMENT

I. LOUISIANA'S ATTEMPT TO TAX APPELLANT'S OUT-OF-STATE ACTIVITIES VIOLATES THE DUE PROCESS CLAUSE OF THE UNITED STATES CONSTITUTION.

A. Louisiana Cannot Tax Transactions Or Property Wholly Beyond Its Jurisdiction.

Louisiana's levy of a use tax upon Holmes for its activities in connection with promotional materials created, paid for, and shipped from out of state constitutes a denial of Holmes' constitutional right to due process under the law, because the State of Louisiana does not have a sufficient nexus or connection with the taxpayer's activities it seeks to tax. The requirement of sufficient nexus between a tax and the transactions within a state upon which the tax is levied is "the most fundamental precondition on state power to tax." *General Motors Corp.* v. *Washingon*, 377 U.S. 436, 450, *reh'g denied*, 379 U.S. 875 (1964) (J. Brennan, dissenting). The Due Process Clause of the Fourteenth Amendment requires "some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax." *Miller Bros. Co.* v. *Maryland*, 347 U.S. 340, 345 (1953), *reh'g denied*, 347 U.S. 964 (1954); *Scripto, Inc.* v. *Carson*, 362 U.S. 207 (1960); *American Oil Co.* v. *Neill*, 380 U.S. 451 (1965). The tax must be applied to "an activity with a substantial nexus with the taxing state." *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. 274, 279, *reh'g denied*, 430 U.S. 976 (1977). Hence, Louisiana must have a sufficient nexus with the activity of the taxpayer it seeks to tax before a tax may properly be imposed.

The Louisiana use tax statute provides that a use tax can be imposed only on "tangible personal property" that is purchased outside of the State of Louisiana, brought into Louisiana and "used, consumed, distributed, or stored for use or consumption" *in Louisiana*. La. Rev. Stat. Ann. § 47:302

(A)(2). A use tax is distinct from a tax upon the property itself. It is a "tax on the enjoyment of that which was purchased." *McLeod* v. *J.E. Dilworth Co.*, 322 U.S. 327, 330 (1944). "[A] use tax, like a sales tax, is an excise or privilege tax different in kind from a tax *on* property." *Sullivan* v. *United States*, 395 U.S. 169, 177 n.28 (1969). Since the tax is imposed upon the *use* of the catalogs, rather than upon the catalogs themselves, Louisiana must have a substantial nexus with that activity. Moreover, the use of the catalogs must sufficiently relate to Holmes in order to withstand constitutional scrutiny. *Henneford* v. *Silas Mason*, 300 U.S. 577 (1937).

The United States Supreme Court has recognized that:

> All States that impose sales taxes also impose a corollary use tax on tangible property bought out of State to protect sales tax revenues and put local retailers subject to the sales tax on a competitive parity with out-of-state retailers exempt from sales tax.
>
> * * *
>
> *But the limitation of use taxes to consumption within the State so as to avoid problems of due process that might arise from the extension of the sales tax to interstate commerce* . . . does not avoid all constitutional difficulties.

National Geographic Society v. *Calif. Bd. of Equalization*, 430 U.S. 551, 555 (1977) (emphasis added, citation omitted).

Implicit within this pronouncement is the principle that a state's attempt to tax beyond its border is invalid as a violation of the Fourteenth Amendment. The rule that a state may tax only that which is within its jurisdiction was first articulated by the United States Supreme Court in 1873 and has never been abrogated:

> The power of taxation, however vast in its character and searching in its extent, is necessarily limited to subjects within the jurisdiction of the State. These subjects

> are persons, property and business. Whatever form taxation may assume, whether as duties, imports, excises or licenses, it must relate to one of these subjects.

Cleveland, Painesville & Ashtabula R.R. Co. v. *Commonwealth of Pennsylvania*, 82 U.S. 179, 186 (15 Wall. 1873).

The rule has been followed without exception. For instance, in *Farmers Loan & Trust Co.* v. *Minnesota*, 280 U.S. 204 (1930), this Court refused to uphold a Minnesota tax assessed upon the testamentary transfer of Minnesota state and municipal bonds issued to a New York resident. The transfer was effected in New York, where the will was probated. In striking down Minnesota's inheritance tax assessment, the Court observed that "no state may tax anything not within her jurisdiction without violating the Fourteenth Amendment." *Id.* at 210.

Similarly, this Court underscored the constitutional limits placed upon a state's power to tax in *Connecticut Gen. Life Ins. Co.* v. *Johnson*, 303 U.S. 77 (1938):

> But the limits of the state's legislative jurisdiction to tax, prescribed by the Fourteenth Amendment, are to be ascertained by reference to the incidence of the tax upon its objects rather than the ultimate thrust of the economic benefits and burdens of transactions within the state. As a matter of convenience and certainty, and to secure a practically just operation of the constitutional prohibition, we look to the state power to control the objects of the tax as marking the boundaries of the power to lay it. Hence it is that a state which controls the property and activities within its boundaries of a foreign corporation admitted to do business there may tax them. *But the due process clause denies to the state power to tax or regulate the corporation's property and activities elsewhere.*

Id. at 80-81 (emphasis added).

The tax at issue in *Connecticut General* was a California franchise tax levied upon gross premiums received from insurance business conducted within California. *Id.* at 78. The taxpayer, a Connecticut insurance company licensed to do business in California, entered into reinsurance contracts in Connecticut with other California insurance companies. California sought to tax these contracts because they reinsured policies issued by the California companies to California residents. Since the reinsurance contracts involved no action taken in California, the tax could not be sustained.[6]

These cases therefore mandate that the use or consumption taxed by Louisiana must occur within the state in order to avoid problems of due process. Although use tax schemes in general are constitutional, such taxes must be imposed with regard to an attribute of property ownership *exercised within the state* by the taxpayer sought to be taxed. *Henneford* v. *Silas Mason Co.*, 300 U.S. 577 (1937). Property acquired or transported in interstate commerce may be subject to a use tax when the article is actually used or is made available for use within the taxing state. *Id.* at 583. Here, there was no use or consumption by Holmes within Louisiana.[7] Holmes' ac-

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[6] *See also Great Atlantic & Pacific Tea Co.* v. *Grosjean*, 301 U.S. 412 (1936), *reh'g denied*, 302 U.S. 772 (1937) ("The state may not tax real property or tangible personal property lying outside her borders; nor may she lay an excise or privilege tax upon the exercise or enjoyment of a right or privilege in another state derived from the laws of that state and therein exercised and enjoyed."); *James* v. *Dravo Contracting Co.*, 302 U.S. 134, 138-139 (1937) (citations omitted) ("As to territorial jurisdiction. — Unless the activities which are the subject of the tax were carried on within the territorial limits of West Virginia [which sought to impose the tax], the State had no jurisdiction to impose the tax. . . . It is clear that West Virginia had no jurisdiction to lay a tax upon [taxpayer] with respect to [its] work done in Pennsylvania."); *ARCO, Inc.* v. *Idaho State Tax Comm'n*, 458 U.S. 307, 315 (1982) ("As a general principle, a State may not tax value earned outside its borders.")

[7] Section 47:301(18) of the Louisiana Revised Statutes Annotated provides:

> "Use" means and includes the exercise of any right or power over

tivities regarding the use and purchase of the catalogs occurred entirely outside the State of Louisiana. The artistic and design work occurred in New York City (Joint App. 70-71, 83-85). At Holmes' direction, New York agencies purchased paper and arranged for the printing and mailing of the catalogs. The catalogs were printed and mailed by the printers from either Atlanta, Boston, or Oklahoma City. (Joint App. 57, 74, 80, 81, 83-87, 88, 90, 91). Holmes sent checks to the post offices in these cities in order to cover postage. (Joint App. 81). It is apparent that every phase of the transaction took place outside Louisiana. The only connnection that linked Louisiana to this activity was the receipt of the catalogs by Louisiana residents. Any use or consumption by Holmes occurred wholly beyond the borders of Louisiana and is therefore beyond the taxing power of that state.

The Louisiana appellate court determined that the taxable use by Holmes consisted of the distribution of the catalogs. "Distribution of the catalogs certainly constitutes 'use' by Holmes under the statute and is subject to the tax." *McNamara* v. *D.H. Holmes Co.*, 505 So.2d at 105. Thus, if "use" is construed as causing the catalogs to be distributed, such use or distribution must have occurred within Louisiana in order to be taxable. It is clear that Holmes' actions in arranging for the purchase, production and printing of catalogs in no way was connected to Louisiana.[8] The remaining phases of the distribution process likewise did not occur

tangible personal property incident to the ownership thereof, except that it shall not include the sale at retail of property in the regular course of business.

[8] Any preliminary activity which may have taken place in Louisiana is not a taxable event because it occurred *before* the tangible personal property which forms the basis of the tax came into existence. A use tax premised upon use or distribution within the state cannot be levied until (1) tangible personal property exists, (2) is purchased out-of-state, (3) is then brought into the state and (4) is used or distributed within the state by the person against whom the tax is to be levied. *See, e.g., Henneford* v. *Silas Mason*, 300 U.S. 577 (1936).

within Louisiana. The act of arranging for the mailing of the catalogs and designating their recipients did not take place within Louisiana. Thus, the Louisiana appellate court upheld the imposition of a use tax on an activity which was conducted entirely outside the state.[9] The tax upon the "distribution" therefore violates the Due Process Clause of the Fourteenth Amendment.

B. The Activity Which Is The Subject Of The Tax Is Not Sufficiently Connected To The Taxpayer Upon Whom The Tax Is Levied.

The consumer or user of the property in this case is the recipient of the catalog, not Holmes. Holmes used the catalogs only while they were located outside the State. By its own terms, the Louisiana use tax law is not intended to "levy a tax on bona fide interstate commerce." La. Rev. Stat. Ann. § 47:305 (5). Indeed, the Louisiana appellate court noted that the taxable moment occurs "when the property has been withdrawn from interstate commerce and has become part of the mass of the property of the taxing state." *McNamara* v. *D.H. Holmes Co.*, 505 So.2d at 105. Withdrawal from interstate commerce and incorporation within the state occurs in this case when the catalogs are placed in the recipient's mailbox. At this moment, Holmes did not possess the power to exercise *any* rights incidental to the catalogs.[10] Thus, the

[9] The State has interpreted its use tax scheme to reach Holmes because any attempt by the State to levy a use tax against the real users in this case, the recipients of the catalogs, would be administratively unworkable. However, Holmes' out-of-state actions in designating the catalog recipients and directing the mailing process did not amount to the type of meaningful use to which the use tax statute is directed.

[10] Once the catalogs are placed in the letter box, any right of Holmes to control the catalogs is extinguished. Federal law prohibits the taking of mail from a letter box, and punishes such taking by fine or imprisonment. 18 U.S.C.A. § 1708.

subject of the tax, use of the catalogs in Louisiana, is not sufficiently connected to Holmes. The fact that Holmes conducts a retail business in Louisiana, and may arguably receive a benefit from the use of catalogs by others in Louisiana,[11] does not eliminate the simple fact that Holmes itself does not use the catalogs in Louisiana within the meaning of the use tax statute.

The Louisiana appellate court recognized that "[t]he thrust of the use tax is that purchasers or users pay taxes on all tangible personal property bought or used within the taxing authority's jurisdiction." *McNamara* v. *D.H. Holmes Co.*, 505 So.2d at 104. However, the court below misapplied this principle to these facts. The law requires "purchasers" to pay taxes on property "bought" within the state, and requires "users" to pay taxes on property "used" within the state. The state court erroneously required Holmes as *purchaser* to pay taxes on property *used* within the state. Louisiana has authority to levy a tax against Holmes as purchaser only on those catalogs purchased within Louisiana. In addition, Louisiana has authority to levy a tax against anyone who used them within Louisiana. Those users were the individual recipients of the catalogs, not Holmes. Clearly then, the activity which is the subject of the tax is not sufficiently connected to Holmes and therefore Louisiana's taxation of that activity violates the Due Process Clause.

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[11] In the Louisiana appellate court, the State asserted that Holmes "used" the catalogs because the Louisiana addressees' use within the State created an indirect benefit to Holmes. The Court of Appeals of Louisiana did not find that any "promotional effect" or indirect benefit to Holmes constituted use by Holmes. *See McNamara* v. *D. H. Holmes Co.*, 505 So.2d 102.

Moreover, the Louisiana statute does not define "use" in terms of indirect benefit. Rather, "use" is defined in terms of the exercise of any right or power of an incident of ownership. *See supra* n.7. No concept of "secondary" or "constructive" use appears in Louisiana's statutory scheme. Holmes lacks any ability to exercise incidents of ownership regarding the catalogs deposited with the United States Postal authorities. Holmes also cannot control whether the property ever reaches its destination.

C. Taxation Of Appellant Is Precluded Because The Appellant's Activities Do Not Have Sufficient Nexus With Louisiana.

The Louisiana appellate court determined that the nexus requirement was satisfied because Holmes operated thirteen stores intrastate. *McNamara* v. *D.H. Holmes Co.*, 505 So.2d at 106. However, a taxpayer's presence within the state does not automatically create nexus sufficient to support taxation of activities which occur outside the state. A taxpayer's in-state activities which are unrelated to the taxed transaction do not create sufficient nexus to properly tax the unrelated activities. *Norton Co.* v. *Dep't of Revenue*, 340 U.S. 534 (1951). The *Norton* rule provides that even if a taxpayer maintains a business within the taxing state, there is no nexus for activities occurring outside the state if the "particular transactions are dissociated from the local business and interstate in nature." 340 U.S. at 537.

Norton involved a Massachusetts manufacturer selling products in Illinois. The taxpayer maintained a branch office in Illinois from which it made local sales at retail. The Illinois office also acted as an intermediary, receiving orders from Illinois residents to be forwarded to Massachusetts, or receiving goods from Massachusetts for shipment to customers within Illinois. The Illinois court held that the presence of the taxpayer's local retail outlet was sufficient to render the taxpayer liable for a direct tax based on the gross receipts of all Illinois sales. *Id.* On appeal, this Court upheld the tax on the direct sales made at retail from the Illinois office, as well as those imposed on transactions where the Illinois office acted as an intermediary. However, the Court excluded all income attributable to orders sent directly to Massachusetts by the customer and shipped directly to the customer in Illinois. The Court refused to uphold the tax on these direct sales because "the State could not reasonably attribute [the] proceeds [of the direct sales] to the local business." *Id.* at 539. Because these transactions were "clearly interstate in character," they were exempted from taxation. *Id.*

Holmes' in-state activities are clearly dissociated from the advertising activities which Louisiana seeks to tax. The act of arranging for the promotion, printing, and mailing of catalogs to Louisiana residents from out of state is a transaction that is "clearly interstate in character." The taxed activity, the "distribution" of the promotional materials, involves the transportation of property from one state to another, as well as transactions and activities between several states.

Subsequent cases have reaffirmed *Norton's* continued viability. In *American Oil Co.* v. *Neill*, 380 U.S. 451 (1965), the *Norton* test was applied to invalidate a state tax on due process grounds. Idaho sought to impose a direct tax on an out-of-state transaction. Although the taxpayer engaged in business in Idaho, the taxed transaction was "entirely unconnected with [the taxpayer's] business in that State." *Id.* at 458. "Each and every phase of the transaction had its locus outside of Idaho. . . ." *Id.* Thus, the tax could not be sustained because there were "no in-state activities connected with out-of-state sales." *Id.*

In *General Motors Corp.* v. *Washington*, 377 U.S. 436 (1964), *overruled on other grounds, Tyler Pipe Industries, Inc.* v. *Washington*, ____ U.S. ____, 107 S. Ct. 2810 (1987), *Norton's* dissociation test was applied to uphold a tax on the privilege of engaging in business levied upon General Motors' gross wholesale sales of products, including General Motors' sale and shipment of cars and parts from outside the state. The Court found sufficient nexus because the taxed activity was "enmeshed in local connections." *Id.* at 447. This Court observed:

> *Although mere entry into a State does not take from a corporation the right to continue to do an interstate business with tax immunity*, it does not follow that the corporation can channel its operations through such a maze of local connections as does General Motors . . . and still maintain that same degree of immunity.

Id. at 448 (emphasis added).

"Dissociation" under the *Norton* standard did not exist in *General Motors* because the taxed transactions "fairly related" to the taxpayer's local business activities. *Id.* at 441. In the instant action, the same direct relationship between the goods shipped into the state and the interstate sales does not exist. There is no way to know what use the recipients make of the catalogs.[12] Many uses may not relate at all to Holmes' in-state sales. Unsolicited advertising distributed free of charge — often termed "junk mail" — frequently goes unopened or is promply discarded without a second thought.

Finally, unlike the activities of General Motors, which consisted of a complex structure of in-state divisions designed to facilitate in-state sales, Holmes' activities were clearly interstate in character. At the heart of the *Norton* rationale is the recognition that purely interstate activities of even an in-state taxpayer should be exempt from taxation. *See Norton Co.* v. *Dep't of Revenue*, 340 U.S at 539. In contrast to General Motors, Holmes did not "channel its operations" through a "maze of local connections." *General Motors Corp.* v. *Washington*, 377 U.S. at 448. The out-of-state activities connected with Holmes' arrangements for the purchase, pro-

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12 The indirect and uncertain nature of any alleged benefit attributable to Holmes serves to distinguish this case from *Standard Pressed Steel Co.* v. *Dep't of Revenue*, 419 U.S. 560 (1975). In *Standard*, a Pennsylvania corporation manufactured and sold products to Boeing, its Washington customer. Standard employed a single employee in Washington whose primary function consisted of the solicitation and procurement of orders from Boeing. Although all orders were placed directly by Boeing to Standard's Pennsylvania location, the employee's in-state activities were singularly targeted to Boeing and directly brought about the sales in question.

Standard may be further distinguished from this case because the nexus analysis in *Standard* pertained to Standard's allegation that Washington lacked sufficient nexus for the imposition of a business and occupation tax. The Court therefore considered whether Standard's obvious business activities within the state were sufficient to permit Washington to exercise jurisdiction over Standard itself (an "entity" nexus inquiry). Instead, this case focuses on a transactional nexus inquiry, that is, Louisiana's nexus with Holmes' *use* of the property.

duction, printing or distribution of the catalogs were separate and independent from its local activity. The distribution of the catalogs was not channeled through Holmes' local presence; such distribution was purely interstate in character. Since Holmes' in-state activities are dissociated from the activites Louisiana seeks to tax, the *Norton* rule precludes taxation in this case.

Because Louisiana lacks sufficient nexus with Holmes' activities conducted outside the state, Louisiana's attempt to tax these activities violates the Due Process Clause. Therefore, the Louisiana Court of Appeal decision should be reversed.

II. THE APPLICATION OF LOUISIANA'S USE TAX TO THE DISTRIBUTION OF INFORMATIONAL CATALOGS THROUGH THE MAIL CONSTITUTES AN IMPERMISSIBLE BURDEN ON INTERSTATE COMMERCE IN VIOLATION OF THE COMMERCE CLAUSE.

The Constitution provides that "Congress shall have Power . . . to regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes." U.S. Const. art. I, § 8, cl. 3. Three of the central purposes of the Commerce Clause are to assure the unrestricted flow of commerce throughout the several states,[13] to insure a national economy free from unjustifiable local entanglement,[14] and to protect commercial intercourse from invidious restraints.[15] Each of these purposes is frustrated by the Louisiana court's decision to uphold the use tax in the case before this Court.

In determining that the tax as levied does not violate the Commerce Clause, the appellate court analyzed the tax under the four-prong test this Court articulated in *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. 274 (1977).[16] Under *Complete Auto*, "[i]f the state tax 'is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fair-

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[13] *Indiana Dep't of State Revenue* v. *Frank Purcell Walnut Lumber Co.*, 152 Ind. App. 122, 282 N.E.2d 336 (1972).

[14] *National Bellas Hess, Inc.* v. *Dep't of Revenue*, 386 U.S. 753 (1967).

[15] *Pennsylvania* v. *West Virginia*, 262 U.S. 553 (1923); *Western Union Tel. Co.* v. *Pendleton*, 122 U.S. 347 (1887); *Robbins* v. *Shelby County Taxing Dist.*, 120 U.S. 489 (1887); *County of Mobile* v. *Kimball*, 102 U.S. 691 (1881); *Welton* v. *Missouri*, 91 U.S. 275 (1876); *Steamship Co.* v. *Portwardens*, 73 U.S. 31 (6 Wall. 1867).

[16] The question of whether the Louisiana Court of Appeal was correct in applying the *Complete Auto* test to this tax on goods in the stream of commerce has been adequately briefed by the parties, and so will not be rediscussed in this brief.

ly related to the services provided by the State,' no impermissible burden on interstate commerce will be found." *Dep't of Revenue* v. *Ass'n of Washington Stevedoring Cos.*, 435 U.S. 734, 760 (1978); *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. 274, 279, *reh'g denied*, 430 U.S. 976 (1977); *Japan Line, Ltd.* v. *County of Los Angeles*, 441 U.S. 434 (1979).

The Louisiana appellate court erred, however, in ruling that the use tax imposed in this case meets *Complete Auto's* fourfold requirements, for on these facts the first requirement is not met. As is discussed previously in Section I of this brief, in this case the tax is applied to activities of the taxpayer which do *not* have a substantial nexus with Louisiana.

Moreover, the facts and issues presented in *Complete Auto* are clearly distinguishable from the facts and issues presented here. The tax at issue in that case was levied for the privilege of carrying on a business in the State of Mississippi. The taxpayer, Complete Auto Transit, Inc., was clearly doing business within the State of Mississippi.[17] Nevertheless, Complete Auto argued that no tax may be applied to an activity that is part of interstate commerce, *even when the taxed activity occurred entirely within the borders of the taxing state. Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. at 278. Essentially, the issue in *Complete Auto* was the degree of immunity from state taxation to be provided to interstate commerce, for the taxpayer in that case espoused the concept that "interstate commerce should enjoy a sort of 'free trade' immunity from state taxation." *Id.* at 278.

Thus, the appellant's sole contention in *Complete Auto* rested on the state's inability to tax *in-state* activity related to interstate commerce as a per se rule and the Court's *Complete Auto* decision is entirely consistent with Holmes' position. In fact, the taxpayer in *Complete Auto* did not make any of the claims asserted by Holmes. Twice the *Complete Auto* Court

[17] The taxpayer was engaged in the business of transporting motor vehicles from railcars in Mississippi to Mississippi dealers. *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. at 276.

noted that the appellant "did not allege that its activity . . . does not have a sufficient nexus with the State . . . [and] it does not claim that discrimination or undue burdens exist in fact." *Id.* at 278.

In contrast, Holmes contests Louisiana's power to levy a use tax on its out-of-state activities which lack a sufficient nexus with Louisiana. Holmes also contests Louisiana's ability to unfairly burden interstate commerce by levying its taxes on the actual movement of mail through the interstate mail system, and the use of that system by a remote sender of mail.

Neither *Complete Auto* nor its progeny have addressed these concerns.[18] Therefore, the conclusions reached in those cases are not determinative of the particular issues presented here.

This Court has repeatedly noted that in subjecting tax statutes to Commerce Clause scrutiny it no longer adheres to formalistic labels, but instead looks to "economic realities" in determining the constitutionality of state taxing schemes. *See, e.g., Moorman Manufacturing Co.* v. *Bair*, 437 U.S. 267, 293 n.7, *reh'g denied*, 439 U.S. 885 (1978); *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. at 279 (1977). In this case, the economic realities of the situation are that it is impossible for Louisiana to tax the real in-state users — the ultimate consumers who receive and use the catalogs in the state within the meaning of the statute. The in-state residents who receive Holmes' promotional catalogs receive the catalogs free of charge. The recipients then "use" the catalogs within the

[18] *See, e.g., Dep't of Revenue* v. *Ass'n of Washington Stevedoring Cos.*, 435 U.S. 734 (1978) (business and occupation tax was properly applied to in-state stevedoring activities in loading and unloading ships' cargo, based on *Complete Auto*); *Commonwealth Edison Co.* v. *Montana*, 453 U.S 609, *reh'g denied*, 453 U.S. 927 (1981) (severance tax upheld on coal mined within state and shipped outside state); *Exxon Corp.* v. *Dep't of Revenue*, 447 U.S. 207 (1980) (for purposes of income taxation, the state assessed a tax based on total income of vertically integrated petroleum company, where company performed marketing activities within the taxing state).

meaning of La. Rev. Stat. Ann. § 47:301 (18) and (19) in a variety of ways.[19] Whether the recipients of the catalogs read them or merely throw them away, it is not feasible for the state to attempt to levy a use tax against the recipients. In an attempt, therefore, to reach a deeper pocket, the State levies a use tax against Holmes for the distribution in Louisiana of the catalogs.

Holmes, however, was *not* the distributor of the catalogs, which were put into the mail by the out-of-state printers and delivered in the State of Louisiana to the recipients by the United States Postal Service. Therefore, the State's taxation of Holmes for the distribution in Louisiana is unconstitutional on due process grounds, as discussed in Section I above. Even assuming for the sake of argument, however, that Holmes was involved in the distribution of its catalogs in the State of Louisiana,[20] then the Louisiana use tax in essence taxes Holmes' use of the United States Postal Service.

This constitutes as direct a burden on interstate commerce as is imaginable. What is essentially being taxed is a person's ability to use the United States Postal Service to communicate to others, as well as the actual movement of the property itself in interstate commerce.

Louisiana claims to be levying its tax on distribution of the

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19 La. Rev. Stat. Ann. § 47:301 provides in pertinent part:

> (18) "Use" means and includes the exercise of any right or power over tangible personal property incident to the ownership thereof, except that it shall not include the sale at retail of that property in the regular course of business.
>
> (19) "Use tax" includes the use, the consumption, the distribution and the storage, as herein defined.

20 Although Holmes is responsible for arranging for the distribution of the catalogs, all of these arrangements were made out of state. Holmes did not exercise *in Louisiana* any right or power over the *tangible personal property* once the tangible personal property existed, as required by La. Rev. Stat. Ann. 47:301(18). See discussion in Section I of this brief.

catalogs by Holmes at a magical "taxable moment" said to exist after the goods have completed their interstate journey and "come to rest" in the resident's mailbox but before the resident plucks them out of the mailbox. *McNamara* v. *D.H. Holmes Co.*, 505 So.2d at 105. This Court, however, has declared its intent to look beyond such formalisms and focus instead on the "practical effect" of the tax statute in question. *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. at 279. In reality, the tax in this case is levied on the movement by the United States Postal Service of promotional catalogs paid for by Holmes, created in New York City, and then printed in and mailed from Atlanta, Georgia, Boston, Massachusetts or Oklahoma City, Oklahoma. (Joint App. 57, 74, 80, 81, 83-87, 88, 90, 91).

The specter of the practical effects of such a tax call to mind the Court's statement in *McGoldrick* v. *Berwind-White Coal Mining Co.*, 309 U.S. 33 (1940):

> Certain types of taxes may, if permitted at all, so readily be made the instrument of impeding or destroying interstate commerce as plainly to call for their condemnation as forbidden regulations.

Id. at 48.

Likewise, in *Miller Bros.* v. *Maryland*, 347 U.S. 340 (1953), *reh'g denied*, 347 U.S. 964 (1954), the Court stated:

> We do not understand the State to contend that it could lay a use tax upon mere possession of goods in transit by a carrier or vendor upon entering the State, nor do we see how such a tax could be consistent with the Commerce Clause.

Id. at 344.

If Holmes is held liable for the use tax because it effected a distribution of catalogs in Louisiana by virtue of arranging for mail to be sent into Louisiana by an out-of-state printer, the printer could also be liable for the use tax because it, as

the actual sender, even more directly effects the allegedly taxable Louisiana distribution. And if both the actual and the putative senders of these catalogs may be held liable for use tax in Louisiana, they and all other commercial senders and putative senders may be made liable for use tax in every state into which they direct promotional, informational or other similar material. That such taxes would place invidious restraints on commercial intercourse is clear, as each entity could be required to track each piece of mail sent. Under the Louisiana appellate court's decision, colleges could be required to pay use tax in Louisiana based upon the percentage of recruiting brochures or alumni fund-raising letters sent to residents there. Similarly, rural hospitals or small rural medical centers seeking doctors, as well as the search firms they engage to assist them in direct mail searches for personnel, could both be held liable for the percentage of the search letters "distributed" in Louisiana, assuming they had the requisite connection with the state to subject them to its taxing power.[21]

Moreover, communication by mail is not the only mode of interstate commerce which stands to be directly and unduly burdened by the Louisiana Court of Appeal's decision. Senders and putative senders of interstate radio, telephone, and television communications sent by cable from one state to another may similarly be liable for use tax in each of the states in which the communciation is received and through which the interstate communication passes.

Once it has been determined that the tax statute in question directly burdens interstate commerce, such burdens must be weighed against the benefit to the state of the challenged tax legislation. Even if the statute imposed only "incidental" burdens on interstate commerce,

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[21] The requisite nexus might be found if, for example, the out-of-state rural hospital is owned by a corporation which owns other hospitals in Louisiana, or if the hospital interviews prospective doctors in the state or participates in medical research there in conjunction with a Louisiana university or medical school.

> the courts must nevertheless strike it down if "the burden imposed on such commerce is clearly excessive in relation to the putative local benefits." Moreover, "the extent of the burden that will be tolerated will of course depend on the nature of the local interest involved, and on whether it could be promoted as well with a lesser impact on interstate activities."

Minnesota v. *Clover Leaf Creamery Co.*, 449 U.S. 456, 471 *reh'g denied*, 450 U.S. 1027 (1981) (citation omitted) (*quoting Pike* v. *Bruce Church, Inc.*, 397 U.S. 137 (1970)).

In this case, the state has no compelling health or safety interests which the challenged legislation protects. Even if the State would increase its revenues by levying the use tax in question, it must not be permitted to do so at the expense of the interests that the Commerce Clause is designed to protect.

Moreover, the State has no argument that Holmes does not already pay its "just share of the state tax burden" for the benefits and protections it receives from the state of Louisiana. *Complete Auto Transit, Inc.* v. *Brady*, 430 U.S. at 279; *Western Live Stock* v. *Bureau of Revenue*, 303 U.S. 250 (1938). Holmes already pays all city and state taxes to which it is subject. (Joint App. 54, 65-66, 98). Holmes pays sales tax on all items it purchases or leases for use in its business. (Joint App. 65-66).[22] Indeed, to the extent Holmes' cost of producing the catalogs is reflected in the cost of goods sold, the State already receives its fair share connected to the in-state use of

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[22] Moreover, Holmes complies with its duty to charge and collect on catalog sales: "[A] tax is collected on any item that is purchased from the catalog. . . . If it's [sic] ordered by mail order form in them, such sales are "very small," only "one to two percent" of Holmes' total sales." (Joint App. 71-72). *National Bellas Hess* v. *Dep't of Revenue*, 386 U.S. 753 (1967), is therefore not applicable to this case. The questions before the Court in *Bellas Hess* concerned whether the requisite nexus existed for Illinois to require an out-of-state mail order house to collect use taxes owed by Illinois residents with respect to merchandise they ordered through the mail order house's catalog.

free promotional materials, for Holmes charges and collects Louisiana's sales tax on all of its retail sales. (Joint App. 128-129). Thus, it is clear that the local benefits to the State, if any, of upholding the challenged use tax are insufficient to counterbalance the excessive burdens on interstate commerce which such a tax entails.

As the analysis above demonstrates, the use tax at issue places invidious restraints on commercial intercourse and impermissibly burdens interstate commerce in violation of the Commerce Clause.

CONCLUSION

The judgment of the court below cannot be sustained under the Due Process Clause because the State of Louisiana seeks to levy a use tax upon an in-state taxpayer for its out-of-state activities. Louisiana's attempt to tax an activity lacking a substantial nexus with the State also violates the Commerce Clause under the *Complete Auto* test. Moreover, the attempt to tax one's ability to communicate through the use of the interstate mail system impermissibly burdens interstate commerce. Clearly then, the Louisiana use tax, as applied in this case, violates both the Due Process and the Commerce Clause of the United States Constitution.

The judgment below should therefore be reversed.

Respectfully submitted,

MARYANN B. GALL
(Counsel of Record)
NANCY TRUITT BLOSSER
LAURA A. KULWICKI
JONES, DAY, REAVIS & POGUE
1900 Huntington Center
41 South High Street
Columbus, Ohio 43215
(614) 469-3939

Counsel for Amicus Curiae

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